

P-421/EM-93-482 ORDER REJECTING PROPOSAL AND REQUIRING REFUNDS

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

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Chair
Commissioner
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Commissioner

In the Matter of a Proposal by
U S WEST Communications, Inc. to
Reduce Digital Switched Service
Rates, Change Options and
Conditions of Service for
Digital Switched Service, and
Establish a Late Payment Charge

ISSUE DATE: January 20, 1994

DOCKET NO. P-421/EM-93-482

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REQUIRING REFUNDS

PROCEDURAL HISTORY

On May 21, 1993 U S WEST Communications, Inc. made a two-part filing proposing to make changes in its Digital Switched Service (DSS) and to establish a late payment charge for all customers. On August 6, 1993 the Company made a supplemental filing revising its original cost and revenue projections.

As to Digital Switched Service, the Company proposed to reduce recurring rates, introduce volume discounts, end individual case pricing, reduce termination liabilities, and reduce minimum service terms. The Company put the changes into effect on May 31, 1993 under Minn. Stat. § 237.60, subd. 2 (a), (d), and (f). That subdivision authorizes the Commission to reinstate the status quo if it finds the new rates do not cover incremental costs or are not just and reasonable.

As to the late payment charge, the Company proposed a 1% charge on any balance of \$50 or more for which payment had not been received by the printing date of the next monthly bill. The Company put the late payment charge into effect on October 7, 1993 under Minn. Stat. § 237.63, subd. 4 (c) and 237.075, stating it would make full refunds if the Commission ultimately disallowed the late charge.

The Company put the proposals together in a single filing so their net effect would be income-neutral.

The Department of Public Service (the Department), the Residential and Small Business Utilities Division of the Office of the Attorney General (RUD-OAG), the Minnesota Business Utility Users Council (MBUUC), and North Star Technical Resources (North Star) filed comments on the Company's proposal.

The Department opposed the DSS rate reduction as unnecessary and contrary to public policy, the income neutrality proposal as illegal, and the late payment charge as in need of refinement. The RUD-OAG supported the DSS rate reduction, opposed the income neutrality proposal, and urged modifications to the late payment charge. The MBUUC supported the DSS rate reduction. The MBUUC and North Star opposed the late payment charge on grounds that the payment interval was unreasonably short.

State Representative Walter E. Perlman appeared at the hearing to oppose the late payment charge proposal. He reported that some of his constituents had been charged late fees after an unreasonably short interval for payment.

The filing came before the Commission on November 30, 1993.

FINDINGS AND CONCLUSIONS

I. Summary of Commission Action

The Company filed the proposed changes in Digital Switched Service and the proposed late payment charge as a package, and the Commission will reject them as a package. The Commission finds the late payment charge too flawed to implement, the income neutrality proposal inappropriate, and the changes in Digital Switched Service not amenable to stand-alone treatment. Each finding will be explained in turn.

II. Late Payment Charge

Late payment charges are unobjectionable when properly designed and implemented. Delinquent accounts impose costs on utilities, and it is reasonable to assign those costs to the customers causing them instead of spreading them over the general body of ratepayers. Late payment charges, however, are subject to the same requirement that they be "fair and reasonable" as other charges imposed by utilities. Minn. Stat. § 237.06. To be fair and reasonable, late fees must be reasonable in amount, assessed only after adequate notice, and assessed only after reasonable opportunity for timely payment. The current proposal fails on all three counts.

First, the Company's proposal fails to establish reasonable, consistent, and clearly stated payment deadlines. The Company proposes to charge a late fee on monthly balances exceeding \$50 not paid in full by the date the next bill is prepared. Since bill preparation times vary from four to eight days, however, customers cannot be certain what that date will be. It is patently unfair to assess a late fee without notifying the customer of the specific date after which it will be assessed.

Furthermore, under the current proposal customers will sometimes be left with an unreasonably short time to pay before incurring a late charge. If preparing the bill takes a full eight days and mail delivery is delayed, customers can have as few as 14 days between their receipt of the bill and the due date. This is clearly an unreasonably short payment period.

Similarly, business customers have raised concerns about the Company's relatively short billing cycles. Most businesses have fixed procedures for recording, verifying, and paying bills which take longer than 14 days. The Minnesota Business Utilities Users Council and North Star Technical Resources therefore suggested deferring late fees for business customers for two billing cycles, requiring the Company to change business billing cycles on request, or similar measures. Clearly, these concerns reflect business realities and need to be addressed.

Finally, U S WEST proposes to assess late charges on all amounts it is entitled to collect from the customer. In some cases this will include long distance charges, charges from information services providers, Alternative Operator Services fees, and other third-party debts. The record does not demonstrate that the Company calculates late fees for third-party services on the basis of U S WEST's liability to the third party. Neither does it establish any reasonable basis for an alternative method of calculation. This, too, is of concern to the Commission.

The Commission rejects the late payment charge proposal for all the reasons set forth above and will require the Company to refund all late payment charges collected to date. The Commission urges the Company to confer with residential customers, consumer advocates, the Department, and business customers of all sizes before submitting another proposal, to make sure it does not raise similar concerns.

III. Income Neutrality and DSS Rates

The Company filed the late charge proposal and the Digital Switched Service proposal as a package so that the two proposals' financial effects would offset each other. Since the Company cannot raise its rates across-the-board while under an incentive plan, it is wary about losing financial ground on any individual rate change during the life of the plan. Therefore, it has typically filed rate change proposals in combinations that make them income-neutral.

A. Income Neutrality and the Incentive Plan

Effective January 1, 1990 U S WEST began operating under an incentive regulation plan approved by the Commission under Minn. Stat. § 237.625 (1992). Incentive regulation is a form of

alternative regulation designed to increase companies' incentives to operate more efficiently. Under incentive regulation a company is allowed to earn amounts in excess of its authorized rate of return, subject to a requirement to return a specified percentage of excess earnings to ratepayers. Companies operating under incentive plans cannot raise their rates except under carefully limited circumstances.

Although companies operating under incentive plans cannot file general rate cases, they may petition to adjust rates for specific services. The Commission may also adjust rates for specific services while a plan is in force. When U S WEST filed its incentive plan it asked for Commission assurance that during the life of the plan all Orders affecting noncompetitive services, and all Orders affecting competitive services in proceedings not initiated by the Company, would be income neutral. The Commission refused, for reasons set forth in detail in the Order accepting and modifying the plan.¹

Basically, there were three reasons for rejection: (1) the effects of guaranteeing income neutrality were too far-reaching and unpredictable; (2) the public expected rate stability to result from the incentive plan; the Company had nurtured this expectation; and the Commission had set the sharing threshold to reflect the financial effects of maintaining rate stability; and (3) guaranteeing income neutrality could act to shield the company from the legitimate risks of competition, especially in proceedings affecting competitive services.

Nevertheless, the Commission did not reject the possibility of income neutrality out of hand:

None of this, however, should obscure the fact that income neutrality will often be appropriate in making miscellaneous rate adjustments over the course of the plan. When the Company desires income neutral treatment, it should submit a specific proposal for achieving it, for review by the Commission and all interested parties.

Order, at 22-23.

As discussed above, the Company has typically filed proposals for achieving income-neutrality with its rate change proposals, and the Commission has typically granted them. In this case, however, the proposal for income neutrality is inappropriate because the lost income falls on the competitive side of the ledger. Making up losses from competitive services by raising

¹ In the Matter of Northwestern Bell Telephone Company's, d/b/a U S West Communications, Proposed Incentive Regulation Plan, Docket No. P-421/EI-89-860, FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER (June 7, 1990) at 20-23.

rates for noncompetitive services is a classic example of the cross-subsidization the Legislature sought to avoid when it authorized streamlined regulation for competitive services:

Cross-subsidization. A telephone company may not subsidize its competitive services from its noncompetitive services through allocations of costs, cost-sharing agreements, or other means, direct or indirect.

Minn. Stat. § 237.62, subd. 2.

The Commission has repeatedly recognized that it would be improper to allow the company to offset competitive losses with noncompetitive rate increases.² In the June 7 Order approving the incentive plan, the Commission declined to guarantee income neutrality in part because "it could operate to insulate the Company from the legitimate risks of competition. . . ." Order, at 22. Later, discussing the potential for cross-subsidization under incentive regulation, the Commission took it for granted that the statute prohibited the course of action the Company proposes here:

If Northwestern Bell [now U S WEST] faces revenue reductions because of rate reductions for competitive services, it is not allowed under law to increase its rates for noncompetitive services to recover those revenues.

Order at 32.

B. Commission Action

The Commission continues to believe that offsetting a reduction in competitive rates (here, Digital Switched Service rates) with an increase in noncompetitive rates (here, the late payment charge) violates Minn. Stat. § 237.62, subd. 2 and will disapprove the income neutrality proposal for that reason. Since the Company has requested approval of the rate reduction only in

² The Commission rejects the Company's claim that an earlier case involving nonrecurring charges is precedent for allowing the Company to offset competitive losses with noncompetitive gains. The purpose of the nonrecurring charge case was to arrive at a just allocation of nonrecurring costs (which translate into nonrecurring charges) between competitive and noncompetitive services. The Commission did not over-allocate to the noncompetitive side to make up a shortfall on the competitive side. In the Matter of a Petition to Restructure Nonrecurring Charges by Replacing Service Charges with Product Specific Charges, Docket No. P-421/EM-91-190, ORDER GRANTING INTERVENTION PETITION, APPROVING CHANGES IN NONRECURRING CHARGES, REQUIRING CUSTOMER NOTICE, AND REQUIRING FURTHER FILINGS (March 26, 1992).

conjunction with its income neutrality proposal, the Commission will reject the proposed rate change and require a return to the rates previously in effect.

Finally, the Company's proposal to re-allocate revenues between competitive and noncompetitive services could be viewed as a rate design proposal requiring examination on its own merits, as opposed to an income neutrality proposal dismissible under the prohibition against cross-subsidization. However, rate design changes of this magnitude, changing existing relationships between competitive and noncompetitive costs and revenues, are beyond the scope of a miscellaneous tariff filing. They require the thorough scrutiny available in a rate case, incentive plan docket, or some equally comprehensive proceeding. For this reason, too, the Commission will reject the Company's proposal.

ORDER

1. The Company's May 21, 1993 proposal to establish a late payment charge and change its Digital Switched Service rate schedule is rejected.
2. Within 10 days of the date of this Order the Company shall file a plan for refunding all amounts collected under the late payment charge disapproved in this Order.
3. Within 10 days of the date of this Order the Company shall file a plan for reinstating the Digital Switched Service rates in effect before the May 31, 1993 rate change.
4. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar
Executive Secretary

(S E A L)